Postal Regulatory Commission
Submitted 2/12/2016 1:44:52 PM
Filing ID: 94985
Accepted 2/12/2016

BEFORE THE POSTAL REGULATORY COMMISSION

WASHINGTON, D.C. 20268-0001

Annual Compliance Report, 2015 **Docket No. ACR2015**

REPLY COMMENTS OF PITNEY BOWES INC.
(February 12, 2016)

Pitney Bowes Inc. (Pitney Bowes) respectfully submits these reply comments in response to the comments filed by the National Postal Policy Council (NPPC) and the National Association of Presort Mailers (NAPM) regarding the workshare prices for First-Class Mail Automation letters.[1]

As a matter of regulatory economics and sound economic policy, the object of worksharing is to minimize the total combined costs of providing postal services by increasing productive efficiency.[2] Postal services can be provided at the lowest combined cost and price if and only if the least cost provider performs the work. The Postal Service should perform upstream postal activities, such as presortation, barcoding, handling and transportation of mail whenever it is the least cost provider. Mailers and mail service providers should perform the work whenever their costs are lower than the Postal Service's. As the Commission has long recognized, setting workshare discounts equal to the (unit) avoided costs is the best way to

[1] *See* Comments of the National Postal Policy Council (Feb. 2, 2016)(NPPC Comments); Comments of the National Association of Presort Mailers (Feb. 2, 2016)(NAPM Comments).
[2] *See* R. Cohen, M. Robinson, J. Waller, and S. Xenakis, "Worksharing: How Much Productive Efficiency, at What Cost and at What Price?" In *Progress Toward Liberalization of the Postal and Delivery Sector*, edited by M. Crew and P. Kleindorfer. New York: Springer (2006).

maximize productive efficiency because mailers and mail service providers will be incentivized to perform the upstream work *if and only if* they are the least cost provider.[3]

The NPPC comments reinforce these important points. From a mailer's perspective, passthroughs less than 100 percent of the avoided cost underprice the Postal Service's upstream sortation services, selling them at less than the cost of providing them and, thus, discouraging the mailer from performing work that the mailer might be able to perform at a lower cost than the Postal Service.[4] NPPC Comments at 5. In NPPC's key example, the Postal Service would sort a First-Class Mail letter from the AADC/3-Digit level to the 5-Digit level at an average cost of 3.6 cents even though the mailer could have performed this same sortation at a cost of 3 cents. *See id*. That is because the Postal Service set the discount at only 2.5 cents. *See id*. Because the work is not being performed by the least cost provider, mail preparation costs and postage costs will be greater than necessary in the larger society.

As the NPPC comments point out, setting workshare discounts below avoided costs is not only bad economics; it is financially self-defeating for the Postal Service. NPPC's example highlights the fact that from a "make or buy" standpoint, the Postal Service incurs 3.6 cents per piece in costs for every piece that it performs the upstream work, when it could have "bought" the same work from the mailer for 3.0 cents. *See* NPPC Comments at 5.

The NAPM comments make the same fundamental point:

> The Postal Service should . . . set workshare discounts equal to avoided costs. That is the only way the Postal Service can improve operational efficiency and lower total mailing costs. These changes would also help grow Presort volumes,

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[3] *See e.g.,* Docket No. ACR2014, Annual Compliance Determination Report (Mar. 27, 2015) at 69 ("The Commission notes that passthroughs below 100 percent send inefficient price signals to mailers. Therefore, it encourages the Postal Service to adjust discounts to bring passthroughs closer to 100 percent."); Docket No. RM2007-1, Order No. 43 (Oct. 29, 2007) at 41 (recognizing that the Commission has used efficient component pricing as a "guiding principle" in rate design to promote productive efficiency).

[4] It is worth noting that under the price cap, any benefit derived from underpriced upstream services is offset by overpriced downstream (delivery) services that the mailer cannot avoid through worksharing.

> increase postal operational efficiency, improve the Postal Service's financial condition, and help drive more mail into the automation mail stream.

NAPM Comments at 3.

As pointed out in the initial comments of Pitney Bowes, inefficient workshare price signals are also contrary to the objective of the modern rate system "to maximize incentives to reduce costs and increase efficiency," 39 U.S.C. § 3622(b)(1), and fail to sufficiently take account the modern rate system factors regarding the "degree of preparation of mail for delivery into the postal system performed by the mailer and its effect upon reducing costs to the Postal Service," 39 U.S.C. § 3622(c)(5), and "the need for the Postal Service to increase its efficiency and reduce its costs, including infrastructure costs, to help maintain high quality, affordable postal services," 39 U.S.C. § 3622(c)(12), among others.[5]

Finally, the NPPC comments correctly observe that setting workshare discounts below avoided costs is "a form of exclusionary pricing taking work away from more efficient private mal preparation firms[.]" NPPC Comments at 5. Pitney Bowes agrees.[6] The antitrust laws do not cover market dominant products; therefore, the Commission must play a more active role to protect fair competition in these upstream markets.

Pitney Bowes joins NPPC and NAPM in urging the Commission to require the Postal Service to set workshare passthroughs at, or as close as practicable to, 100 percent of the costs avoided. Doing so would promote efficiency, lower the total combined costs for mailers, and encourage the retention and growth of its most profitable products. While the statute provides sufficient authority for the Commission to fully address this issue at this time, Pitney Bowes

[5] *See* Initial Comments of Pitney Bowes (Feb. 2, 2016) at 5.

[6] *See id.*, at 5 n.4 (citing Docket No. ACR2011, Comments of John C. Panzar on behalf of Pitney Bowes Inc. (ACR2011 Panzar)(Feb. 3, 2012) at 5 ("Reducing discounts below Postal Service avoided costs for any reason is a form of exclusionary pricing. This vertical price squeeze would exclude more efficient competitors from performing upstream services. This would have a short-term negative effect on the productive efficiency.").

recognizes the limitations on the scope and timing of the Commission's annual compliance determination may make that difficult.[7] Those same limitations will not apply to the mandatory 10-year review of the modern rate system, *see* 39 U.S.C. § 3622(d)(3); therefore, the 10 year review will provide an appropriate proceeding to address these concerns.

Pitney Bowes appreciates the Commission's consideration of these comments.

Respectfully submitted:

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[7] *See e.g.,* Docket No. ACR2011, Annual Compliance Determination Report (Mar. 28, 2012) at 102 ("Panzar's analysis, . . . is beyond the scope of this proceeding. The issue of whether the Commission's rules governing workshare discounts should be modified may be pursued, if appropriate, in a rulemaking proceeding.").